

BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Market Dominant Product Prices
Standard Mail
PHI Acquisitions, Inc.

Docket No. MC2014-21

Market Dominant Product Prices
PHI Acquisitions, Inc. (MC2014-21)
Negotiated Service Agreement

Docket No. R2014-6

PUBLIC REPRESENTATIVE INITIAL COMMENTS
(April 23, 2014)

I. Executive Summary

The Postal Service has entered into a market dominant NSA with PHI, and requests the Commission's approval to implement the agreement. There are three statutory requirements for market dominant NSAs. First, the NSA must improve the net financial position of the Postal Service. Second, the NSA must not cause unreasonable harm to the marketplace. Third, the NSA must be available on public and reasonable terms to similarly situated mailers.

The core concept of the agreement with PHI builds upon over a decade of industry experience in leveraging mailer response to create value for both mailers and the Postal Service. The PHI NSA is functionally equivalent to the NSA with Bookspan filed in 2005, and this shared core concept furthers the public interest and is a sound basis for moving forward with declining block market dominant NSAs. However, as set forth in these comments, the Postal Service has not provided the information needed to determine that the PHI NSA comports with the requirements of the law. The Postal Service has not provided data necessary to understand the financial impact of the NSA.¹ The Postal Service has not provided any information regarding how the NSA can be expected to

¹ Despite repeated attempts by the Commission, the Postal Service has not provided the mailer specific information required by 39 CFR 3010.42(c). The major difference between the PHI NSA and the Bookspan NSA is the discount cap, as further discussed in Section III.

impact the competitive marketplace. Additionally, the Postal Service has added unneeded complexity to the process for PHI's competitors and other similar mailers to obtain similar agreements.

The Postal Service has entered into an agreement with PHI that is similar to agreements that the Commission has approved in the past, but the Public Representative is unable to find that implementation of the agreement is lawful and furthers the public interest without an alteration and additional data to hedge against the substantial risk to Postal Service capital that this agreement creates. While review of this NSA should be a straightforward endeavor, the combination of complexity, errors, and delay has created an uncertain and incomplete record. The following comments aim to highlight areas that the Commission, before approving, and the Postal Service, before implementing, should address. With the additional information, transparency, safeguards, and accountability envisioned by these comments, the Public Representative would support implementation.

II. BACKGROUND

The core concept of the PHI market dominant NSA² (PHI NSA) is a straightforward declining block discount, where the discount increases as the mailer increases its volume. The Postal Service indicates that the agreement is designed to increase the total contribution the Postal Service receives from PHI Standard Mail Carrier Route Flats volume and revenue by generating new, incremental Standard Mail Carrier Route Flats volume and revenue. The agreement is scheduled to last 5 years. The Postal Service describes the agreement as containing four main components: (1) a volume threshold, (2) a volume threshold adjustment, (3) a volume commitment, and (4) rebates on qualifying Standard Mail Carrier Route Flats volume.

Specifically, the volume threshold is based on the amount of PHI's total volume for

² On March 5, 2014, the Postal Service filed a request pursuant to 39 U.S.C. 3622 and 3642, as well as 39 CFR 3010 and 3020, *et seq.*, to add a PHI Acquisitions, Inc. (PHI) negotiated service agreement to the market dominant product list. In Order No. 2009, the Commission established the Docket Nos. MC2014-21 and R2014-6 and appointed the undersigned Public Representative. In Order No. 2009, the Commission established a comment deadline of March 27, 2014.

On March 20 and 21, 2014, the Commission issued CHIRs No. 1 and 2. The Postal Service filed a complete response to CHIRs No.1 and 2 on April 3, 2014. Due to errors and missing information, the Commission issued CHIR No. 3 on April 11, 2014. The Postal Service filed its response on April 16, 2014. In Order No. 2049, the Commission extended the initial comment deadline to April 23, 2014.

all four categories of Carrier Route Flats (Saturation, High Density Plus, High Density, and Basic), as well as Flats Sequencing System (“FSS”) Flats with a full- service IMb barcode. If PHI exceeds the quarterly volume threshold in any quarter, it will earn rebates on its qualifying Standard Mail Carrier Route Flats volume, as detailed in the following table.

TIER	Volume Increase Above Quarterly Baseline Threshold	Rebate
Tier A	Up to 10%	10% off published rates at the time of mailing
Tier B	10.01 to 18%	15% off published rates at the time of mailing
Tier C	Above 18%	20% off published rates at the time of mailing

There is a long list of additional contract terms. Among them are as follows: (1) an acquisition clause, which accounts for the acquisition of another company or catalog title; (2) a divestiture clause, which accounts for decreased mailing activity due to the divestiture of a catalog title; (3) a termination clause, which allows either party to end the agreement with 30 days written notice to the other party, based on certain conditions, including a package volume commitment by PHI; (4) an option to renew clause, which allows the parties to renew the agreement for up to five additional years if specified criteria is met; and (5) an incentive programs clause, which allows PHI to participate in Postal Service incentive programs while preventing PHI from double-collecting on incentives. Notice at 9-10.

III. FINANCIAL ANALYSIS

The contract signed by the Postal Service is 14 pages, with an additional 9 pages of “Mail Classification Changes” filed by the Postal Service with its Notice. The inherent complexity of the contract and the Postal Service’s ongoing lack of explanation have made the potential financial impact of the PHI NSA difficult to understand and the Postal Services calculations impossible to replicate.

There are three different sets of calculations provided by the Postal Service that predict the outcome of the NSA. The first set of calculations was provided by the Postal

Service when it first filed its request. Initially, the Postal Service estimated that the NSA would increase total contribution by \$10.7 million. The second set of calculations was provided on April 8, 2014, in response to CHIR No. 1 question 11, wherein the Postal Service changed all of its calculations and projections for the NSA as result of the exigency adjustment provision included in the original contract. With its revised set of calculations, the Postal Service estimates that the agreement will increase contribution by over \$13.2 million. The third set of calculations was provided on April 16, 2014 in response to CHIR No. 3, when the Postal Service correctly utilized the Commission's approved methodology for estimating the financial impact of NSA. Under this set of calculations, the Agreement is estimated to achieve a positive net financial benefit of \$1.5 million in contract year 1. Due to the complexity of the contract terms, it is impractical to estimate net financial impact beyond the first contract year.

Postal Service March 5, 2014 Original Filing

Table 1 details the Postal Service's initial projections for the PHI NSA.

Table 1: USPS Projection of PHI NSA Financial Impact – Original Filing

Postal Service's Initial PHI NSA Projections				
	USPS Projected Before Rates Volume	Threshold Volume	USPS Projected After Rates Volume	USPS Projected Net Financial Impact
Contract Year 1	197,332,400	202,626,000	243,000,000	\$ 1,279,398
Contract Year 2	196,101,046	208,474,069	266,000,000	\$ 1,700,085
Contract Year 3	194,877,375	216,806,550	274,000,000	\$ 2,087,282
Contract Year 4	193,661,341	225,090,873	281,000,000	\$ 2,491,166
Contract Year 5	192,452,894	233,189,165	287,000,000	\$ 3,190,536
				\$ 10,748,465

Evaluating each of these columns is a useful endeavor to gain a practical understanding of the complex contractual mechanisms.

PHI Volume Projection –Absent Implementation of the Agreement

Before Rates volumes are the volumes that the Postal Service anticipates PHI will mail absent the agreement. While these projections have no material impact on the outcome of the NSA, the Postal Service's projection of Before Rates volume is important because the Postal Service uses these volumes as the baseline for determining its profit from the agreement.

The following table details the volume history of PHI, as reported by the Postal

Service.

**Table 2: PHI Historical
Volume**

	<u>PHI Volume</u>			
	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>
Total Potpourri Group NSA	198,247,804	199,171,686	200,943,161	202,626,000

As mentioned by the Postal Service, PHI has a very steady mailing history, with year to year growth of less than 1 percent. In its initial filing, Postal Service projected that, without an NSA PHI will reverse its 4 year trend and begin to experience volume declines, as detailed in the table below.

Table 3: USPS Projection of PHI Volume Absent Agreement –Original Filing

	<u>USPS Projected Before Rates Volume</u>					
	<u>2014 (Proj)</u>	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>	<u>Year 5</u>
Total Potpourri Group NSA	201,500,000	197,332,000	196,101,000	194,877,000	193,661,000	192,453,000
Projected Change	-0.56%	-2.07%	-0.62%	-0.62%	-0.62%	-0.62%

The Commission requested an explanation for this projection in CHIR No. 1 question 10. Specifically, in its Notice the Postal Service stated PHI's eligible volume is projected to "increase by about 1 percent" per year without an NSA, which would be consistent with historical growth, but not the Postal Service's workpapers. In its response, the Postal Service states that Notice "should have stated 'decrease' rather than 'increase.'"³ The Postal Service provided a qualitative discussion regarding its expectation that PHI will change course and begin a 6 year period with a negative volume trend absent implementation of the NSA. The Postal Service noted that that it "adjusted for statistical outliers...adjusted for recent catalog acquisitions...adjusted for growth in Carrier Route volume as a percentage of the total volume... [and] tracked the most recent volumes for Standard Mail Flats and Carrier Route Flats." The Postal Service summarizes the process, stating "the adjustments were made judgmentally, based on experience."⁴

The Postal Service mentions several quantitative factors used to develop what appears to be a very precise growth rate of -0.62 percent during years 2-5 of the

³ Postal Service Response to CHIR No. 1 Question 10 at unnumbered page 1. Filed April 8, 2014

⁴ Postal Service Response to CHIR No. 1 Question 10 at unnumbered page 2. Filed April 8, 2014.

agreement. The workpapers the Postal Service used to develop this estimate would be helpful in assessing the validity of the method and estimate. The Postal Service has not made available documentation that details the calculation of its PHI volume projection.

Threshold Volume Calculation

The Threshold Volume is an essential component of the agreement. As the Public Representative understands, the “Adjustment Factor” incorporates the success of the previous year’s prospecting into the baseline volume, while excluding the effects of unsuccessful prospecting. In contract, the calculation of the “Adjustment Factor” is detailed as “ 0.00898×16.13 , or 0.145.” In the Postal Service’s workpapers, cell E209 of tab “1_Inputs” of file “PHI_NSA_Financials.xls” contains an “Adjustment Factor” of 0.1448. It is unclear what number of significant digits will be used for the “Adjustment Factor” when it is applied.

Public Representative Recommendation #1: The Postal Service should clarify how the “Adjustment Factor” will be applied.

The contract contains a very detailed provision that allows the Postal Service to review and revise the two variables that are used to calculate the “Adjustment Factor.” As such, it is unclear if the “Adjustment Factor” will be 14.5 percent for the duration of the contract.

Postal Service Projection of PHI Volume with NSA Implementation

The Postal Service projected PHI would mail 243 million pieces in Contract Year 1 and steadily increase volume to 287 million pieces by Contract Year 5. The Postal Service has provided no documentation for the development of these estimates; they are hard coded numbers in the Postal Service’s workpapers. In response to CHIR No. 1 Question 8, the Postal Service stated “Qualitative and quantitative analysis was performed using PHI historical trends, and other macroeconomic variables (income or GDP, sales trends, volume trends in the catalog industry, etc.) that tend to correlate with PHI mail volume.”

Ultimately, the Postal Service’s estimates of what will occur are not material to the outcome of the NSA, as the actual volumes mailed pursuant to the agreement will define the impact of the agreement. Past experience with mailer specific discounts has

shown that accuracy of such projections is low.⁵

USPS Projected Net Financial Impact

The Postal Service has proposed (without making a formal proposal) to use a different methodology for estimating the net financial impact of the NSA. As it has in the past, the Postal Service prefers to compare the projected results of the NSA with its projection of what the mailer would have done, absent any agreement. Table 5 details the calculation of the projected impact for contract year 1.

Table 4: Postal Service Methodology for Calculation of Net Financial Impact – Contract Year 1 –Original Filing

Contract Value	
Projected Volume	243,000,000
Before Rates Volume	197,332,400
Incremental Volume	45,667,600
Contribution	\$ 2,501,497
Earned Rebates	\$ 1,222,099
USPS Net Value	\$ 1,279,398

Note that the key number in this calculation, Incremental Volume, is a function of the Postal Service's undocumented projection of Before Rates volume.

Postal Service April 8, 2014 Revised Filing

The Postal Service signed the Agreement with PHI on January 23, 2014. On January 26, 2014, the "exigent" prices resulting from Docket No. R2013-11 went into effect. In CHIR No.1, question 11, the Commission noted that Section III.D of the agreement contains a provision that would alter the Annual Volume Threshold and Baseline volumes in the event of implementation of above-CPI rate increases. On April 8, 2014, the Postal Service confirmed that the threshold and baseline volume revision provisions of the contract had been activated by the January 26, 2014 price increases, and filed new workpapers reflecting that change. Table 6 contains the Postal Service's revised projections of the financial impact of the PHI NSA.

Table 5: USPS Projection of PHI NSA Financial Impact – Revised Filing

⁵ See Docket No MC2004-3 Data Collection Report, which details that the Postal Service's projection of contract year 3 volume was 340 million less than the actual volume, even though no discounts were provided. <http://www.prc.gov/Docs/63/63373/Chase.EoY3.Report.Complete.pdf> See also Docket No MC2005-2 Data Collection Report, which details that the Postal Service's projection of contract year 3 volume was 400 million more than the actual volume, leading to no discounts. <http://www.prc.gov/Docs/62/62763/HSBC.EOY.Report.08.Complete.pdf>

Postal Service's Initial PHI NSA Projections				
	USPS Projected Before Rates Volume	Threshold Volume	USPS Projected After Rates Volume	USPS Projected Net Financial Impact
Contract Year 1	184,170,000	189,112,000	227,000,000	\$ 1,564,301
Contract Year 2	183,021,000	194,599,978	248,000,000	\$ 2,150,817
Contract Year 3	181,879,000	202,334,833	256,000,000	\$ 2,615,462
Contract Year 4	180,744,000	210,108,093	262,000,000	\$ 3,084,785
Contract Year 5	179,616,000	217,624,500	268,000,000	\$ 3,832,876
				\$ 13,248,242

All of the volumes, both baseline and projected, were revised downward. The projected net financial impact increases by nearly \$3 million as a result of the revision.⁶ The mechanics of the revision for Contract Year 1 are detailed in table 7.

Table 6: Contract Year 1 Revision for Exigency Adjustment Factor

	Original	Exigency Adjustment Factor	Revised
USPS Projected Before Rates Volume	197,332,400	-6.67%	184,170,000
Threshold Volume	202,626,000	-6.67%	189,112,000
USPS Projected After Rates Volume	243,000,000	-6.58%	227,000,000
Projected Incremental Volume	45,667,600		42,830,000
Contribution	\$ 2,501,497		\$ 2,762,471
Rebate	\$ 1,222,099		\$ 1,198,169
USPS Projected Net Financial Impact	\$ 1,279,398		\$ 1,564,301

The key to the Postal Service's revision is the adjustment factor of 6.67 percent. In CHIR No. 3, the Commission requested the calculations used by the Postal Service to develop the estimates and projections in table 6. The Postal Service provided the file "ExigencyAdi_CHIR3Q3.xlsx." The Postal Service notes that "this analysis was done jointly with PHI and the vendor." The calculations of this adjustment are detailed in table 8.

Table 7: Revised Annual Volume Threshold for Exigent Provision

⁶ The increase in projected value after including the revenue from the exigent prices is a reminder of both the Postal Service's pricing power and the value of offering NSAs to mailers who enter profitable mail. Due to the exigent price increase, the contribution per piece from PHI's volume will increase from 5.5 cents to 6.4 cents per piece. Even though the Postal Service's incentivized volume declines, the overall value of the agreement increases.

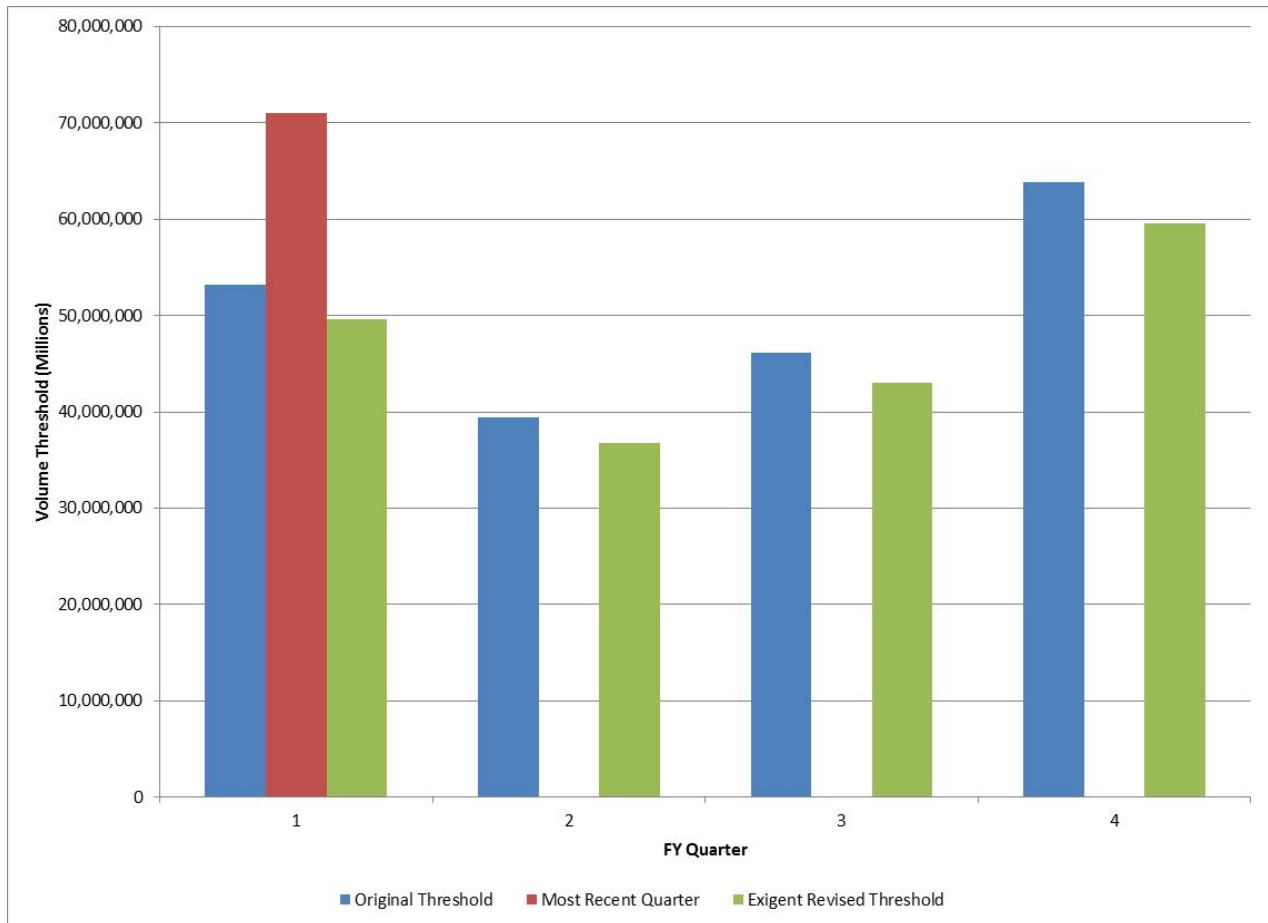
Original Contract Annual Volume Threshold	202.626
Volume for the Most Recent 4 Quarters - Jan 13 to Dec 13	220.449
Total Annual Postage for the contract provision period	\$49,954,182
Increased Total Annual Postage for the same period	\$53,133,154
Increase Percentage	6.36%
January CPI-U preceeding the rate change	1.60%
Less the CPI-U	4.76%
Factor	1.4
Adjustment Percentage	6.67%
Revised Annual Volume Threshold	189.112

This calculation, and the information used therein, raises several questions. First, the Postal Service did not use billing determinant data to develop this figure. Instead of using the actual mailer specific volume for the whole year and the actual change in price, the adjustment factor was developed using a “sample of selected mailing events.” The Postal Service’s inability to provide historic billing determinant data in an NSA proceeding is unprecedented. From the original Capital One NSA to the recent Discover NSA, the Postal Service has provided rate category level volume data. Given the PHI mail must bear a Full Service IMb, it is unclear what is preventing the Postal Service from providing the data necessary to replicate PHI’s volume history and the impact of the exigent prices on that volume.

Public Representative Recommendation #2: The Postal Service should provide billing determinant data for PHI from FY 2013 Q1 to FY 2014 Q1 to ensure Volume Thresholds are accurately calculated.

Second, PHI has increased its volume by nearly 18 million in the most recent quarter. Chart 1 contains PHI volume from FY 2013 Q1 to FY 2014 Q1 and the Adjusted Quarterly Thresholds using the information provided in “ExigencyAdi_CHIR3Q3.xlsx.”

Chart 1: PHI Historical Quarterly Volume and Exigent Revised Volume Thresholds



If the agreement is implemented, in FY 2015 Quarter 1, the volume threshold will be just less than 50 million pieces. In FY2014 Quarter 1, which was not used for the calculation of the volume threshold in the original contract, PHI mailed over 70 million pieces. Similar to the Postal Service's recent experience with the Discover NSA, it appears that PHI is increasing its volume well in advance of implementation of the NSA. This is also an extremely relevant data point for examining the Postal Service's projection of PHI volume absent the implementation of the NSA. In order for PHI to mail 188 million pieces in FY 2014, as projected by the Postal Service, PHI would have to decrease its volume by over 22 percent for the rest of this year, compared to last.

In addition to understanding the mechanics of the revision, it is important to understand why the revision occurred. The contract signed by the Postal Service on January 23, 2014, contained specific volume thresholds; Section III.B contains a very specific Contract Year 1 Volume Threshold of 203.626 million pieces, as well as very specific quarterly thresholds. The workpapers originally filed by the Postal Service in

this docket reflect the Postal Service's estimate of how the NSA would unfold, starting with that volume baseline (which is PHI's historical volume). The agreement also contains a provision to downwardly adjust the volume threshold in the extremely predictable scenario of an exigent price increase. On January 23, 2014, the Postal Service was fully aware that such an event would occur in 3 days. When the Postal Service filed its workpapers the exigent prices had been in effect for over a month. The Postal Service took nearly 3 weeks to develop revised workpapers, stating that the workpapers were filed late "because of the need for internal review and verification of the data contained in the requested financial workpapers, both by the Postal Service and its contract partner."⁷

The Postal Service's Motion For Late Acceptance suggests that the Postal Service had not analyzed the financial impact of the PHI NSA with the contractual adjustment for the exigent prices prior to requesting regulatory approval. It also suggests that PHI and the Postal Service had yet to agree to the new volume thresholds resulting from the exigent prices. A complicating factor of the exigency provision is the Commission's ruling in Docket No. R2013-11 that the exigent prices can be implemented for a limited period of time. The Postal Service has not clarified if the discount thresholds will be adjusted when the exigent surcharge is removed.

Public Representative Recommendation #3: The Commission require the Postal Service to clarify how the PHI discount thresholds will be adjusted when the exigent surcharge is removed.

Postal Service Revised Projection of After Rates Volume

As in its original workpapers, the Postal Service's revised projection of both Before Rates and After Rates volumes are hardcoded and unexplained. The Postal Service notes that it has adjusted its Before Rates and After Rates volumes by the same exigency factor used to adjust the baseline volume and discount thresholds. The following table details this adjustment.

Table 8: Postal Service Revision of Before Rates and After Rates Projections

⁷ Motion of the United States Postal Service for Late Acceptance of Response to Chairman's Information Request No. 1 Questions 10-11.

Before Rates Volume - Adjusted for Exigency				
Year 1	Year 2	Year 3	Year 4	Year 5
197,332,000	196,101,000	194,877,000	193,661,000	192,453,000
184,170,000	183,021,000	181,879,000	180,744,000	179,616,000
-6.67%	-6.67%	-6.67%	-6.67%	-6.67%

After Rates Volumes -Adjusted for Exigency					
	Year 1	Year 2	Year 3	Year 4	Year 5
Original Projection	243,000,000	266,000,000	274,000,000	281,000,000	287,000,000
Revised Projection	227,000,000	248,000,000	256,000,000	262,000,000	268,000,000
Percent Change	-6.58%	-6.77%	-6.57%	-6.76%	-6.62%

PHI increased its volume by over 33 percent in FY 2014 Q1 compared to FY 2013 Q1, yet the Postal Service predicts that volume will decline to under 185 million (7.5 percent before accounting for the FY 2014 Q1 volume increase), with the implementation of exigent prices in contract year 1. The Postal Service has not made available documentation that supports this projection. In Docket No. R2013-11, the Postal Service estimated that the implementation of exigent prices for all of FY 2014 would decrease Carrier Route, High Density, and Saturation volume by less than 2 percent.⁸

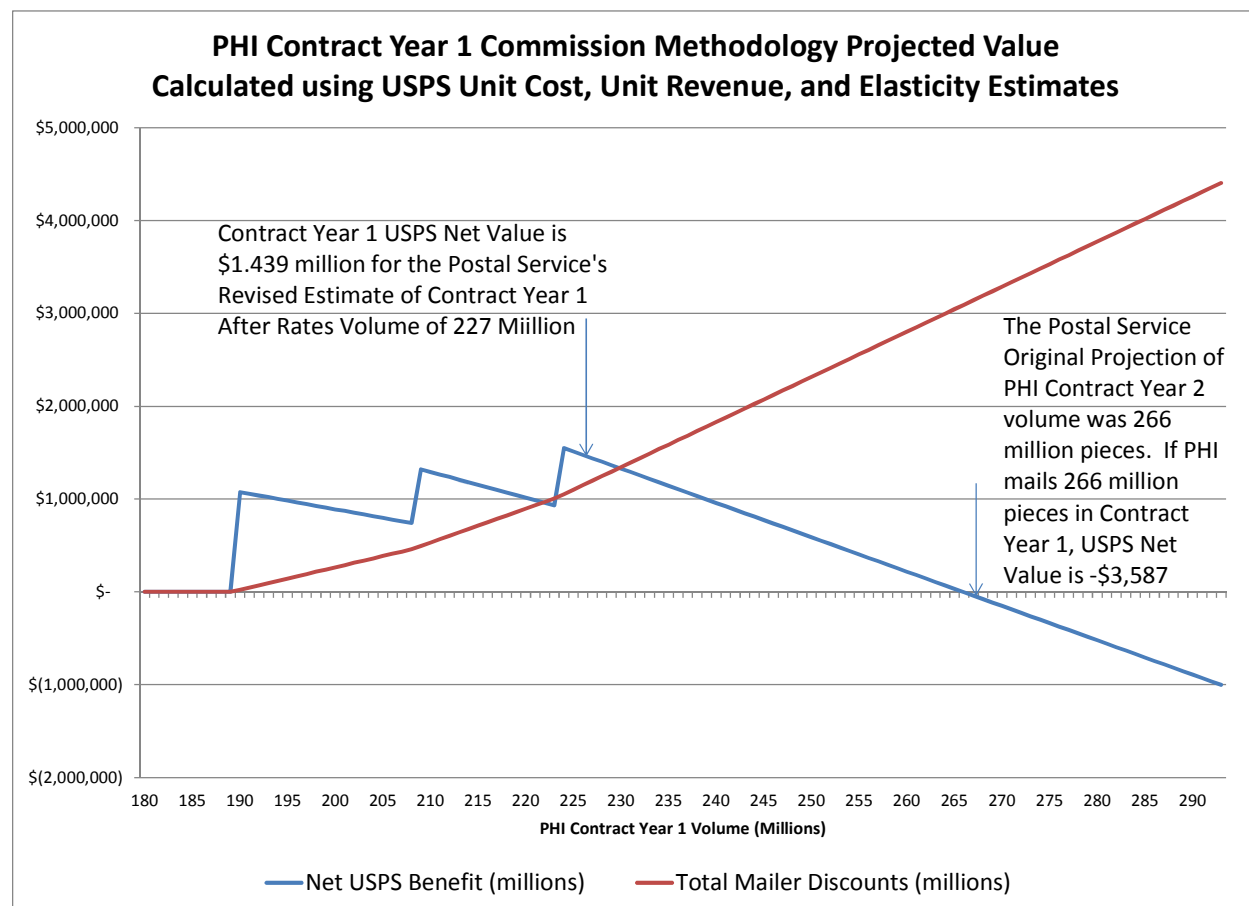
Commission Approved Methodology for Estimation of Net Financial Impact

The accepted Commission methodology is used to isolate the impact of the NSA rebates on Postal Service finances. The purpose of the Commission methodology is to estimate mailer response to a lower price using quantitative inputs. The accepted methodology incorporates a projection of contract year 1 rebated volume, the marginal rebate, and the Standard ECR own-price elasticity.⁹ The following chart contains a projection of the impact of the NSA across a range of potential outcomes.

Chart 2: Range of Potential Contract Year 1 Outcomes Using Commission Methodology

⁸ See Docket No. R2013-11 Nickerson workpapers file "Nick.Statmnt.Attach.Rev.11.22.13.xls" tab "Attach 12 2014 Cont AR 10-1-13" cells D19-21 and tab "Attach 26 2014 10-1" cells D19-21.
<http://www.prc.gov/Docs/88/88358/Nick.Statmnt.Attach.Rev.11.22.13.xls>

⁹ The Postal Service's estimates of elasticity reflect subclasses, rather than products, that were used prior to the PAEA. ECR refers to Enhanced Carrier Route. It includes the following commercial products: Carrier Route, High Density and Saturation Letters, and High Density and Saturation Flats and Parcels. The accepted methodology was developed in Docket No. MC2004-3. The 2013 Standard Mail ECR elasticity is -0.890, as provided in the attachment to the January 20, 2014 letter from Andrew German.



As detailed in the chart, the PHI NSA can be expected to have a positive financial impact in Contract Year 1 for the range of 185 million to 265 million pieces.

Interestingly, the estimate of the net financial impact for contract year 1 using the commission's methodology is within \$100,000 of the Postal Service's estimate for the same projected volume. As briefly discussed earlier, this NSA has many desirable characteristics. Standard Mail ECR is profitable for the Postal Service and the elasticity is high, suggesting that an NSA could add value for both the mailer and the Postal Service.

Public Representative Recommendation #4: The Commission utilize its approved methodology to evaluate the financial impact of the PHI NSA.

Using the Commission's methodology with the information provided by the Postal Service, it appears that the PHI NSA will have a positive benefit.¹⁰ Furthermore, there is

¹⁰ Using billing determinant data is essential for the accuracy of the Commission's methodology, as unit cost and unit revenue are pivotal in the calculation.

a demonstrable risk that if the volume threshold has been set too low, PHI could mail volume sufficient to eliminate the positive benefit of the NSA, and possibly create considerable harm to Postal Service capital.

The PHI NSA is analogous to the Bookspan NSA, Docket No. MC2005-3. For that NSA (and the functionally equivalent NSAs with Bradford Group and Lifeline Screening), the Postal Service capped the discounts that Bookspan could obtain in any given contract year. Applying a discount cap in this docket would provide substantial protection for the mailing community and general public, limiting the potential negative impact for any given contract year.

Public Representative Recommendation #5: The Commission utilize its approved methodology to develop a Discount Cap for each Contract Year.

It is especially important for the Postal Service to cap the yearly discounts for PHI in light of PHIs acquisitions policies.¹¹ PHI is short for PHI Acquisitions.¹² As experienced in the Docket No. MC2004-3 Bank One/ Chase NSA, improper implementation of a merger can lead to sizable financial losses.¹³ The design of this NSA increases such concerns. PHI has, according to the Postal Service, historically achieved over 90 percent Carrier Route or deeper presorted mail. According to the ACMA, the industry average for catalogs is 70.5 percent.¹⁴ If PHI acquires another catalog company, the Postal Service will adjust the volume threshold for the acquired companies NSA eligible volume (Carrier Route, High Density, High Density Plus, and Saturation). If PHI is able to convert mail formerly entered at 5-digit prices to Carrier Route in a merged mail stream, the volume threshold adjustment will not accurately account for such a change in worksharing, rather than volume growth.

In response to CHIR No. 1 question 10, the Postal Service stated that it adjusted its projection for future PHI volume absent the implementation of the NSA for PHIs recent catalog title acquisitions. The Postal Service has a plan for adjusting for corporate changes, and it should provide that plan to the Commission to ensure, if

¹¹ See <http://multichannelmerchant.com/news/potpourri-group-acquires-fetchdog-11062012/>, <http://www.themiddlemarket.com/news/potpourri-group-buys-cuddledown-236585-1.html>

¹² <http://investing.businessweek.com/research/stocks/private/snapshot.asp?privcapId=46952973>

¹³ See Year Three Periodic Data report at 14. <http://www.prc.gov/Docs/63/63373/Chase.EoY3.Report.Complete.pdf>

¹⁴ See Docket No ACR2012 ACMA Initial Comments at p. 4 footnote 5. <http://www.prc.gov/Docs/86/86390/ACMA%20Initial%20Comments%20ACR2012.pdf>

activated, it is applied properly.¹⁵

Public Representative Recommendation #6: The Commission require the Postal Service provide its analysis of the historical impact of PHI Acquired and Divested titles on volume.

IV. UNREASONABLE HARM TO THE MARKETPLACE

The Postal Service has paid scant attention to the legal requirement that the NSA not cause “unreasonable harm to the marketplace.” In response to CHIR No. 1 question 3, the Postal Service stated that it “expect the contribution from mailers not party to the Agreement will not change as a result of this Agreement.” The Postal Service has provided no basis for this expectation. The Postal Service is providing one mailer with substantial postage discounts, and expecting that mailer to increase its volume substantially over the next 5 years. PHI competes with other catalogers who may not be able to get the same discounts. The Postal Service’s failure to provide any analysis of the marketplace should not be accepted as an affirmative showing that the NSA will not cause unreasonable harm.

Public Representative Recommendation #7: The Commission require the Postal Service to provide an affirmative showing that the PHI NSA will not cause unreasonable harm to the marketplace.

A few million dollars in postal discounts are unlikely to disrupt the global marketplace for apparel, but for smaller marketplaces the effect may be much more pronounced. PHI operates in number of niche marketplaces. If there are only two catalogs that offer earth-friendly personalized dog collars¹⁶, it is much more likely that some unreasonable (or avoidable) harm will result from this NSA. And such harm would be easily preventable, as the Postal Service the NSA must be available on public and reasonable terms to similarly situated mailers.

If the only other catalog mailer that specializes in earth friendly personalized dog collars contacts the Postal Service in an attempt to reach a similar agreement, the Postal Service should pursue such an agreement in order to maintain marketplace

¹⁵ In the book “The Irrational Economist” (Public Affairs 2010, Eds. Kerjan, E and Slovic, P), Economist Paul Kleindorfer discusses the importance of “legitimation theory” in economic decision-making. Succinctly, if economic actors are required to show the process for decisions with an understanding that future decisions will be judged based off of that process, better processes result and implementation improves.

¹⁶ PHI Catalog “In the Company of Dogs” sells such collars for \$19.95.

fairness, as envisioned by PAEA.

The Postal Service states that all of the complexities of the contract will be essential when determining if other mailers will be considered for similar agreements, and that additional element would also be considered, stating “all key aspects of this Agreement (will) be used in determining whether another mailer is deemed to be ‘similarly situated’ to PHI... Furthermore, additional elements would be considered that may be applicable to other mailers, including the various components of the termination clause in this Agreement.”¹⁷ With previous NSAs, the Commission has required the Postal Service to report about mailers that have approached the Postal Service for a functionally equivalent NSA. See Docket No. MC2002-2 Capital One Data Collection Report.¹⁸ In those dockets, the Postal Service was required to report on the “number of requests made for comparable NSAs” and the “status of negotiations, or if negotiations were terminated, the reason (s) therefore.”

Public Representative Recommendation #8: The Commission should require the Postal Service report on the number and status of negotiations for functionally equivalent NSAs.

¹⁷ Postal Service Response to CHIR No. 1 Question 7. <http://www.prc.gov/Docs/89/89495/Resp.CHIR.No.1.Q1-9%20and%2012.pdf>

¹⁸ http://www.prc.gov/Docs/42/42783/data_coll_rpt_sep_03_-_sep_04_final.pdf

V. CONCLUSION

In these comments, the Public Representative has respectfully outlined 8 areas that deserve further exposition and consideration before the Commission dispenses with this docket. Applied correctly, NSAs have the potential to improve the value of the mail for mailers and the Postal Service alike. As envisioned by PAEA, mailer specific agreements with unneeded complexity available to a select few provide limited benefits while risking much. With improved focus, the PHI NSA has the potential to progress declining block discounts into the PAEA era. The Postal Service has the responsibility to fulfill the requirements of the law before implementing Market Dominant NSAs.

Respectfully Submitted,
/s/ John P. Klingenberg
John P. Klingenberg
Public Representative

901 New York Avenue, N.W., Suite 200
Washington, DC 20268-0001
(202) 789-6863; Fax (202) 789-6891
e-mail: klingejp@prc.gov